

**IT 02-10**

**Tax Type: Income Tax**

**Issue: Responsible Corporate Officer – Failure to File or Pay Tax**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
CHICAGO, ILLINOIS**

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**THE DEPARTMENT OF REVENUE  
OF THE STATE OF ILLINOIS**

**v.**

**JOHN DOE,  
as Responsible Officer of  
ABC Corp.,  
Taxpayer**

**No.**

**01-IT-0000**

**NOD No. 0000**

**FEIN No. 00-0000000**

**Tax Period: 3Q, 4Q, 1999**

**Kenneth J. Galvin**

**Administrative Law Judge**

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**RECOMMENDATION FOR DISPOSITION**

**Appearances:** Mr. William F. Kelley, on behalf of JOHN DOE, Mr. George Foster on behalf of the Department of Revenue of the State of Illinois.

**Synopsis:**

This matter comes on for hearing pursuant to JOHN DOE' (hereinafter "John Doe") protest of Notice of Deficiency No. 0000 (hereinafter "NOD"), as responsible officer of ABC Corp. (hereinafter "ABC"). The NOD was issued for unpaid Illinois withholding tax and covers the third and fourth quarter of 1999. A hearing was held in this matter on May 9, 2002, with Joe Blow, Vice-President of XYZ Company, Jane Doe, Vice-President of MMM Company, and JOHN DOE providing oral testimony. Following submission of all evidence and a review of the record, it is recommended that NOD No. 0000 issued against John Doe be finalized as issued. In support thereof, the following "Findings of Fact" and "Conclusions of Law" are made.

**Findings of Fact:**

1. The Department's *prima facie* case, inclusive of all jurisdictional elements, is established by the admission into evidence of NOD No. 0000, dated November 29, 2000, issued against JOHN DOE, showing a withholding tax liability for ABC in the amount of \$20,333.81 for the third and fourth quarter of 1999. Tr. pp. 8-9; Dept. Ex. No. 1.
2. ABC sold products and services to hospitals, health systems and large and small physician groups. Tr. p. 11; Taxpayer Ex. No. 1.
3. ABC was wholly owned by CCC, Inc. ("CCC"). A letter from XXX, CCC, to XXX, President of ABC, dated February 23, 1999, states that the board of directors of ABC will be composed of XXXX, XXXX and XXXX, *inter alia*. The letter lists three officers of ABC: XXXXX, Chairman and CEO, XXXX, Senior VP Technology, and XXXX, Senior VP Services. The letter states that CCC will fund ABC on the 1<sup>st</sup> and 15<sup>th</sup> of each month, beginning March 1, 1999. Tr. pp. 13-16; Taxpayer's Ex. No. 2.
4. A business plan for "CCC-ABC, Inc." dated October 9, 1999, lists XXXX and XXXX and 5 others as the "management team." Tr. pp. 20-21; Taxpayer's Ex. No. 1.
5. ABC's management meetings were attended by Jane Doe, XXXX, XXXX and JOHN DOE. Tr. pp. 18, 27, 37-38, 46.
6. XXX & Associates did consulting and medical billing and worked closely with a New York company, called "ABC Point," which wrote software called "XXX." XXX & Associates installed and trained clients on the "XXX" software. XXX & Associates and ABC decided to merge their operations and XXXX asked John Doe to join ABC in December, 1998. At that time, John Doe was an independent contractor and did the bookkeeping and tax preparation for XXX & Associates. Tr. pp. 53-54.

7. Prior to becoming an employee of ABC in April of 1999, John Doe reviewed the February 23, 1999 letter from XXXXX to XXXXXX, including the funding schedule. Tr. pp. 56-58; Taxpayer's Ex. No. 2.
8. ABC's initial funding from CCC was timely and at the agreed amounts. At the beginning of June, funding from CCC continued, but only at 60% to 80% of the agreed amounts. By August, 1999, the funding was substantially reduced. The last wire transfer was received in October, 1999. Tr. pp. 60-62.
9. On August 30, 1999, John Doe prepared a "Cash Requirements Report," for a meeting attended by XXX, Jane Doe and others. The report lists "overdue payroll taxes for 7/99" of \$52,101 and "payroll taxes for 8/99" of \$57,395. Tr. pp. 62-63; Taxpayer's Ex. No. 18.
10. John Doe signed the IL-941, "Illinois Quarterly Withholding Income Tax Returns," for quarters ending June 30, 1999 and September 30, 1999. John Doe prepared the IL-501 forms for monthly payroll tax deposits, and prepared and signed the quarterly withholding tax returns for ABC. Tr. pp. 66-68, 88; Taxpayer's Ex. No. 7 and 9.
11. John Doe was paid \$50/hour for working at ABC. On an annual basis, for a 40-hour work week, the salary would be \$108,000. Beginning June 1, 1999, John Doe worked many 40 hour weeks. He stopped working 40 hour weeks in August or September, 1999, when he was no longer getting paid. When John Doe was hired, he was not given stock options or an equity interest in ABC. Tr. pp. 71-71, 83-84.
12. John Doe' duties at ABC included the following: processing accounts payable and payroll checks; preparing and signing accounts payable and payroll checks; monitoring the cash account and advising management of the liabilities and cash requirements; preparing financial statements and financial reports; interfacing with health insurance companies in order to get health insurance for ABC employees. Tr. pp. 85-86.

13. The "NUC-1, Illinois Business Registration" for ABC lists John Doe as "Chief Financial Officer." On Section 2 of the NUC-1, "Sales Tax and Reseller Registration," John Doe accepted "personal responsibility for the filing of returns and the payment of taxes due" in Question 14. Tr. pp. 87-88, 101.
14. No monthly payroll tax deposits were made by ABC for July, August, September, October and November of 1999. Tr. pp. 88-89.
15. John Doe prepared and signed a check for July, 1999, payroll taxes due in August, 1999. No other ABC officer countersigned the check. After that, he did not prepare any more checks for payroll taxes. After August, 1999, John Doe continued to prepare and sign checks for rent, payroll and other expenses. These checks were countersigned by other officers. Tr. pp. 90-93.

### **Conclusions of Law:**

The sole issue to be decided in this case is whether JOHN DOE should be held personally liable for the unpaid withholding tax of ABC. The personal liability penalty is imposed by Section 3-7 of the Uniform Penalty and Interest Act, which provides as follows:

Any officer or employee of any taxpayer subject to the provisions of a tax Act administered by the Department who has the control, supervision or responsibility of filing returns and making payment of the amount of any trust tax imposed in accordance with that Act and who willfully fails to file the return or to make the payment to the Department or willfully attempts in any other manner to evade or defeat the tax shall be personally liable for a penalty equal to the total amount of tax unpaid by the taxpayer including interest and penalties thereon. The Department shall determine a penalty due under this Section according to its best judgment and information, and that determination shall be prima facie

correct and shall be prima facie evidence of a penalty due under this Section.  
35 ILCS 735/3-7.

It is clear under the statute that personal liability will be imposed only upon a person who: (1) is responsible for filing corporate tax returns and/or making the tax payments; and (2) “willfully” fails to file returns or make payments.

The admission into evidence of the NOD establishes the Department’s *prima facie* case with regard to both the fact that John Doe was a “responsible” officer and the fact that he “willfully” failed to file and or pay. Branson v. Department of Revenue, 168 Ill. 2d 247, 262 (1995). Once the Department has established a *prima facie* case, the burden shifts to the taxpayer to overcome the case. Masini v. Department of Revenue, 60 Ill.App.3d 11 (1<sup>st</sup> Dist. 1978).

In determining whether an individual is a responsible person, the courts have indicated that the focus should be on whether that person has significant control over the business affairs of a corporation and whether he or she participates in decisions regarding the payment of creditors and disbursal of funds. Monday v. United States, 421 F.2d 1210 (7<sup>th</sup> Cir. 1970), *cert. denied*, 400 U.S. 821 (1970). Liability attaches to those with the power and responsibility within the corporate structure for seeing that the taxes are remitted to the government. *Id.*

I conclude, based on the testimony and evidence admitted at the evidentiary hearing, that John Doe was a responsible party under the statute. John Doe signed “IL-941’s” for the second and third quarters of 1999. Taxpayer’s Ex. Nos. 7 and 9. On the “IL-941” for the second quarter of 1999, John Doe listed his title as “CFO” or “Chief Financial Officer.” Taxpayer’s Ex. No. 7. John Doe admitted on cross-examination that he also listed himself as “chief financial officer” on the “NUC-1.” Tr. p. 88. On question 14 of the “NUC-1,” concerned with the payment of sales tax, John Doe accepted “personal responsibility for the filing of returns and the payment of taxes.” Tr. p. 83.

ABC’s bylaws are not in evidence, and the record does not show what duties and responsibilities were vested in the office of “chief financial officer.” The “chief financial officer” of a corporation is usually charged with the financial management of the corporation and there is no reason to assume that this is not the case with

ABC. In fact, John Doe' testimony shows that he was in charge of the financial management of ABC. John Doe testified that his duties included processing accounts payable and payroll checks, preparing and signing checks, monitoring the cash account and advising management of cash requirements and preparing financial statements. Tr. pp. 85-86.

John Doe testified that he had check writing authority. "I would apply my signature to the checks and then give them to generally XXXXX but occasionally XXXXX for the second signature." Tr. pp. 59-60. According to John Doe, "two signatures were required on all checks." Tr. p. 59. John Doe argued that he was not responsible because he was never able to get a countersignature on the check for payroll taxes:

Q. Why was the July payroll tax deposit not made? Is that because you couldn't get a second signature on the check?

A. Yes, that's correct.

Q. During the same time period, were you able to obtain countersignatures on other checks that you prepared?

A. Yes.

Tr. p. 89.

No bank signatory cards or check approval authorizations were admitted into evidence for any quarter included in the NOD, so I am unable to verify that two signatures were required. Without bank signatory cards as evidence, I am also unable to verify which officers were authorized to sign. Checks were admitted into evidence that show a space for two signatures. Taxpayer's Ex. Nos. 12 and 14. Assuming that two signatures were required, I must question why John Doe signed other checks when he could not obtain a second signature on the July payroll tax deposit. When the July payroll deposit check was not countersigned, John Doe did not issue or sign any additional payroll tax deposit checks "because everybody knew it wasn't going anywhere until the [July] check was sent... that would have been sent first." Tr. pp. 89-90.

If two signatures were required on checks, this does not relieve John Doe of responsibility, as he argued. What it does do is make him equally responsible with the other signatories for ensuring that taxes were paid. In any corporation, there may be more than one responsible officer. Monday v. United States, *supra*. The

statute does not confine liability to only one person in the corporation or to the person most responsible. 35 ILCS 735/3-7. As the Department's counsel argued in closing, if a corporate officer could deflect responsibility by saying I prepared and/or signed the check but somebody else had to sign it as well, no officer would ever be responsible. Tr. p. 109. The ability to sign corporate checks is a significant factor in determining whether a person is a responsible party because it generally comes with the ability to choose which creditors are paid. Gold v. United States, 506 F. Supp. 473, (E.D.N.Y. 1981), aff'd, 671 F. 2d 492 (2d Cir. 1982). In continuing to sign checks for expenses other than the payroll deposits, John Doe was in fact participating in decisions regarding the payment of creditors and disbursement of funds, signifying that he was a responsible officer of ABC.

Throughout his testimony, John Doe attempted to underplay his position and responsibilities at ABC. John Doe was not on the board of directors of ABC and he was not listed as an officer in a letter from CCC to ABC dated February 23, 1999. Taxpayer's Ex. No. 2. He was not included in the "management team" in the "CCC-ABC, Inc." business plan dated October 9, 1999. Taxpayer's Ex. No. 1. John Doe was not given stock options or an equity interest in ABC. Tr. pp. 70-71. In closing argument, John Doe's counsel characterized him as "much more of an accounts payable clerk than he was a chief financial officer." Tr. p. 125. John Doe testified that "[T]he reason why it was kind of humorous, a joke, that I was the chief financial officer is because I was the only finance person there at all. There was no other accounting clerks or accounts payable clerk or payroll clerk or anybody." Tr. pp. 54-55.

John Doe' testimony as to his lack of responsibility at ABC is self-serving and not credible. First of all, the statute does not require that a responsible officer be on the board of directors, or be a member of the "management team," or have an equity interest in the company. 35 ILCS 735/3-7. Both Joe Blow and Jane Doe testified that John Doe attended management meetings. Tr. pp. 18 and 38, respectively. In fact, Mr. Blow testified that he would not have considered the listing of the "management team" as "inaccurate if it had listed Mr. John Doe there." Tr. p. 27. John Doe has a Bachelor of Science degree in accounting and was a certified public accountant. Tr. p. 50. Prior to coming to ABC, he had 8 years of progressively responsible experience at "Rehabilitation Medicine Clinic," where he started as "project accountant," and "ultimately [he] became the controller." Tr. p. 51. John Doe was knowledgeable about taxes: "I always requested that we pay the payroll taxes because I knew that even if the company were to go into bankruptcy, that that liability would not be

discharged.” Tr. p. 76. Although his attorney characterized John Doe as “more of an accounts payable clerk,” his salary, annualized, was \$108,000, obviously far beyond that of a clerk. Tr. pp. 83-84.

John Doe testified that the last wire transfer that ABC received from CCC was in October, 1999. Tr. p. 62. According to John Doe, he resigned on November 19, 1999, because “[T]here was no company left. There was no money. There was no outlook for having any more money. There was no point sticking around.” Tr. pp. 61, 69. Incredibly, John Doe testified that after his supposed resignation, he wrote a letter to the Illinois Department of Revenue, dated January 31, 2000, which states: “Enclosed is the 4<sup>th</sup> quarter 1999 IL-941 form for ABC Corp., Inc. I am sending this to you despite the fact that nobody associated with the corporation is willing to sign the return. Please advise me as to what course of action I should take.” Taxpayer’s Ex. No. 11. John Doe testified that XXX asked him to prepare the letter “because she was getting a large number of phone calls from former employees wondering where their W-2’s were.” “I told her that – initially that I would not do it since I was no longer employed with ABC Corp., and she managed to talk me into doing it.” Tr. p. 69.

No documentary evidence was admitted showing that John Doe had resigned. XXX was not called as a witness, although the Department’s counsel stated in closing that the State had taken her deposition and “the indication would be that she was available within this jurisdiction to testify.” Tr. p. 102. John Doe’ letter dated January 31, 2000, and the complete lack of documentary evidence concerning the resignation prevents me from concluding that John Doe did in fact resign from ABC. Based on the testimony and evidence admitted at the evidentiary hearing, I must conclude that John Doe had significant control over the financial affairs of ABC over the entire period covered by the NOD, and that by signing checks, he participated in the payment of creditors and disbursement of funds. Accordingly, John Doe has failed to rebut the Department’s *prima facie* case, that he was a responsible person under the statute.

The second element which must be met in order to impose personal liability is the willful failure to pay taxes. The Department presents a *prima facie* case for willfulness with the introduction of the NOD into evidence. Branson, *supra*. The burden then is on the responsible parties to rebut the presumption of willfulness.

“Willfulness” as used in the statute may indicate a reckless disregard for obvious or known risks. Monday v. United States, 421 F.2d 1210 (7<sup>th</sup> Cir. 1970), *cert denied*, 400 U.S. 821 (1970). Willfulness also includes



“failure to investigate or to correct mismanagement after having notice that withholding taxes have not been remitted to the Government.” Peterson v. United States, 758 F. Supp. 1209 (N.D. Ill. 1990). A person acts willfully in failing to pay delinquent taxes if he prefers other creditors to the State. Department of Revenue v. Heartland Investments, 106 Ill. 2d 19 (1985).

John Doe’ conduct was willful under each of the above. John Doe was asked on cross-examination why he continued “to prepare checks and sign checks for expenses other than payroll taxes when [he] knew that the payroll taxes were not being paid.” He responded:

Because I was assured that we would have the money to pay  
the payroll taxes at the time that the – no later than the time  
that the quarterly payroll tax returns would need to be filed.  
Tr. p. 94.

In relying on the assurances made to him, John Doe recklessly disregarded the obvious risk that the money from CCC would not be raised and the withholding taxes due to the State would subsequently not be paid.

John Doe testified that at the beginning of June, 1999, funding from CCC continued but only at 60% to 80% of the agreed amounts. By August, 1999, the funding was substantially reduced and the last wire transfer from CCC was received in October, 1999. Tr. pp. 60-62. According to John Doe, on August 13, 1999, he prepared and signed a check for July withholding, due August 15, 1999, and presented it to XXX for countersignature. Tr. p. 66. “Every single time that we would cut a check for anything, I would ask if we could pay the payroll taxes.” Tr. p. 65. “[XXX] said that we didn’t have the money to pay the taxes at that time.” Tr. p. 68. John Doe was obviously on notice that withholding taxes were not being paid. John Doe did not call XXX as a witness so I am unable to conclusively determine that she refused to countersign the July payroll tax deposit, or that she prioritized disbursements. Without bank signatory cards, I am unable to determine that XXX’s signature was even required on ABC’s checks. No evidence was presented at the hearing to show what steps John Doe took to correct ABC’s mismanagement. No documentary evidence was presented to show any attempt by John Doe to retain enough money in the bank, by court order if necessary, to cover the unpaid withholding taxes, while he continued to wait for a countersignature or additional funding from CCC.

Finally, John Doe repeatedly testified that he continued to sign and obtain countersignatures for checks for expenses other than the withholding taxes:

Q. During the period of time that you were not preparing payroll

tax checks for ABC, that is, from July through the time you left ABC in November, did you continue to prepare checks for rent and other expenses?

A. There were some, yes.

Q. And did you sign those checks?

A. I believe I did.

Q. And what did you do after you prepared and signed those checks?

A. I gave them to [XXX].

...

Q. During the time that the payroll taxes were not being paid for ABC Corp., did you continue to prepare checks to pay actual payroll?

A. Yes.

Q. And did you sign those checks?

A. Yes.

Q. And did you give those to someone for countersignature?

A. Yes.

Q. So, in essence, certain bills were being paid or were given priority – certain expenses were given priority over the payment of the payroll taxes between the beginning of June and the time you left ABC.

A. Yes.

Q. And you were aware that this was going on?

A. Yes.

Tr. pp. 92-93.

John Doe admitted that he prepared, signed and obtained countersignatures for checks for other disbursements during the two quarters covered by the NOD when the State was not paid its withholding taxes. John Doe' testimony clearly shows that other creditors were preferred over the State, further indicating willfulness. Accordingly, John Doe has failed to rebut the Department's presumption of willfulness.

WHEREFORE, for the reasons stated above, it is my recommendation that Notice of Deficiency No. 0000 be finalized as issued.

ENTER

June 13, 2002

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Kenneth J. Galvin  
Administrative Law Judge

